

## Investment Outlook 3rd Quarter 2009



### Highlights:

- Money market 'swap rates' are climbing which will result in better returns from cash
- Our view of investment grade corporate bonds has moderated following a drop in some yields.
- Investors will have to get used to a more volatile stockmarket generating lower long-term returns in the future.
- Our outlook for emerging markets remains more optimistic than developed markets

## About Informed Choice

Informed Choice Ltd works with individual clients and small business owners to help them to build, manage and protect their wealth.

By turning complex personal finance issues into simple plain English solutions, we ensure that our clients are always fully in control of their money.

As one of only five IFA firms in the UK to hold the Gold Standard for Independent Financial Advice we excel not just in service but in all areas important to consumers of financial products and services.



We are a firm of Chartered Financial Planners. This means we have satisfied rigorous criteria relating to professional qualifications and ethical good practice. It means you can be confident that you are dealing with one of the UK's leading firms that is wholly committed to providing you with the best possible advice, service and support.

Our Quarterly Investment Report sets out our views on the general investment climate and creates a robust framework for our investment advice decisions. It also enables us to make tactical alterations to our strategic asset allocation models.

To find out more about our investment advice process please visit [www.informedchoice.ltd.uk/investment.htm](http://www.informedchoice.ltd.uk/investment.htm).

## Introduction

**Martin Bamford BA (Hons) CFP APFS**  
**Chartered Financial Planner**



Welcome to this edition of our Investment Outlook report. We publish this document once a quarter to record the findings and thoughts of the Informed Choice Investment Committee.

The general economic outlook remains varied, with the Organisation for Economic Co-operation and Development (OECD) now predicting that Britain will not enter recovery next year, in contrast to the rest of the world where 0.7% growth is predicted in 2010.

Figures just published by the Office for National Statistics (ONS) show that recession in the UK started earlier than previously thought, in the second quarter of 2008 rather than the period from July to August. The UK economy contracted sharply in the second quarter of 2009 with a fall of 2.4% compared to an expected fall of 1.9%.

At our Investment Committee meeting this quarter we agreed to start making several enhancements to our already robust investment advice process. These include holding our meetings monthly rather than quarterly to reflect changing global market conditions and outlooks. We also plan to develop a series of model portfolios based around our cautious, moderate and aggressive risk profiles.

More frequent Investment Committee meetings will result in more regular reporting of our findings and views. You can keep up to date with these by visiting our blog ([www.informedchoice.ltd.uk/news/blog.htm](http://www.informedchoice.ltd.uk/news/blog.htm)) or subscribing to our free weekly personal finance ezine ([www.informedchoice.ltd.uk/news/ezine.htm](http://www.informedchoice.ltd.uk/news/ezine.htm)).

We hope you find this report interesting and I would personally welcome your feedback. You can email me at [martin@icl-ifa.co.uk](mailto:martin@icl-ifa.co.uk) or call me on 01483 274566.

Regards,

*Martin*

Chairman  
Informed Choice Investment Committee

## Meet the Investment Committee

### **Martin Bamford BA (Hons) CFP APFS**

Martin is a Chartered Financial Planner and Certified Financial Planner (CFP) certificant. He is the author of *Brilliant Investing* which was published by Prentice Hall Business and became WHSmith Business Book of the Month.

In addition to his existing investment qualifications, Martin is currently studying for the Investment Management Certificate (IMC) from the CFA Society of the UK.



### **Dermott Whelan FCCA ASIP DipPFS**

Dermott was a founding member of Morgan Stanley's Discretionary Management team within its Private Wealth Division in 1999 and launched their guided open architecture multi-manager investment platform in 2007. In 2008, as part of the Investment Solutions Group at Fidelity International, Dermott was responsible for manager selection with a focus on European Equity and asset allocation.

Dermott is a Certified EFFAS Financial Analyst and an Associate of the CFA Society of the UK. He is a Fellow of the Chartered Association of Certified Accounts and holds the CII Diploma in Financial Planning.



### **Andrew Neligan BSc (Hons) CFP DipPFS**

Andrew is a graduate of Aston University where he holds an honours degree in Managerial and Administrative Studies. He is a Certified Financial Planner (CFP) certificant and is in the process of applying to become a Chartered Financial Planner.

Andrew holds the CII Diploma in Financial Planning which includes specialist qualifications in Savings and Investments as well as Investment Options at Retirement.



### **Philip Sullivan BA (Hons) CertPFS**

Philip is a graduate of the Polytechnic of Central London where he studied Business and Economics. He has been an independent financial adviser with Informed Choice since 1994. Philip holds the CII Certificate in Financial Planning in addition to a specialist qualification in Investment Principles, Markets and Environments.

Philip is an experienced residential property investor having built up a buy to let portfolio in Guildford and London over the past ten years.



## Summary

- Cash
- Fixed interest securities
- UK Equities
- Overseas Equities
- Property
- Current House View
- The Small but Important Print

## Cash

Money market 'swap rates', which determine the cost of fixed rate mortgages and savings deals, are on the up which has a knock-on effect on the returns available from cash. However, interest rates are starting from a historically low position and we do not expect to see the Bank Rate improve significantly this year. Cash remains the asset class of choice for capital preservation. Investors with money in cash can expect to receive meagre returns for the near future but with the ability to sleep soundly at night.

Economic outlook drives inflation which drives interest rates. Our expectations are for rather benign inflation through into 2010 as various factors including higher taxes, higher unemployment (North America up to 8.5% currently and heading higher) and low wage increase demands conspire to keep consumer confidence low. We cannot underestimate the impact of such a low Bank Rate and inflation is likely to emerge at some point, history tells us that policymakers are usually slow to cut rates and slow to put them back up again.

We remain 'neutral' on this asset class as we believe it is too soon to become overweight and the capital preservation purpose of cash within a volatile investment market makes it too important to become underweight.

## Fixed Interest Securities

Corporate bond fund managers have moderated their views of this asset class recently. We feel that there is still value to be had from investment grade corporate bonds but valuations are less attractive than three or six months ago. The additional yield 'pick up' over UK Government bonds has tightened from an additional 4.5% per year for AA rated corporate bonds, to 3.2%. If this reduces to 2%, which we think is likely, a price gain of 5% will be achieved, in addition to the running yield.

The greater opportunity now exists in high yield (junk) bonds, yield 'pick up' is over 10% per annum, but as we view UK Corporate Bonds as a low-risk asset class we are reluctant to move portfolios into this end of the credit spectrum, where risk levels and volatility are comparable with equities. We remain overweight investment grade bonds and note the importance of asset class correlation when managing a portfolio which also contains equity investments, so tend to avoid too much high yield.

UK government Gilt yields have been pushed up sharply in the past month as a result of fears over excessive government issuance. Ten year yields are now expected to reach 6% with UK government finances in a pretty sorry state. When inflationary pressures do emerge, as a result of a low Bank Rate and quantitative easing, there will be even more pressure on UK Gilts. We remain underweight but recognise their safe haven status.

Our outlook moves from overweight to neutral for international corporate bonds as fluctuating exchange rates pushes more cost through into these funds which hedge against currency fluctuations. We remain neutral on UK index linked bonds as 5 year real yields at 1.6% are fairly valued in our opinion.

*“There is 100% chance we will see inflation and it may be hard to contain”.* - **Warren Buffet**

## UK Equities

Corporate earnings in this asset class remain sector dependent, but are generally improving as a result of write-offs. As we met, the FTSE 100 has been through two negative weeks as investors skimmed off some profit after a reasonable rally since mid-March. The UK stockmarket has more than 20% in oil and gas companies (BP, RD Shell, BG Group), so is supported currently by a relatively high oil price.

It remains unclear whether what we have experienced since mid-March is a bull or bear market rally. Over the longer term we expect investors will have to get used to the concept of more volatile returns from equities and possibly lower total returns over the long term.

Our house view for UK Equities is neutral.

## Overseas Equities

European Equities continue to look good value and the Euro has weakened against Sterling by around 4% since our last Investment Committee meeting. We expect several factors, including archaic employment laws and the diverse nature of member economies, to hold back recovery and for this reason we are underweight.

The United States was the first into the recession and looks set to be one of the first out. We question whether the recent rally seen in this market is sustainable, but the US economy has received massive assistance from the Treasury.

The whole world is dependent to some extent on the US property market which has limited supply/demand underpin when compared to the UK. Our house view of US Equities is overweight, the equity market will price in this economic recovery six to nine months before it happens.

The Japanese stockmarket looks set for a record quarterly gain with the MSCI Asia Pacific Index look set to return a 29% gain for the second quarter of 2009. However, companies on this index trade at nearly 24 times estimated net income which means you pay significantly more for their perceived growth prospects compared to Europe and the UK and to a lesser extent North America.

Our outlook for emerging markets remains more optimistic than developed markets, but this view comes with the strong warning that there are many risks to consider e.g. geopolitical and heavy dependence on a global economic recovery.

Our house view of Japan and Asia Pacific remains 'neutral' and our house view of Emerging Markets is overweight.

## Property

Our focus within this asset class is on UK bricks and mortar, with a specific focus on blue-chip tenants. We noted that the cost of funding might be increasing with money market swap-rates on the rise but availability of finance also appears to be improving.

We have probably seen the worst in this asset class but there could still be bad news to come. Our house view for Property is to remain underweight as we do not expect any form of rapid recovery for this asset class as occupancy rates will also be under pressure.

## Current House View

Asset Class	Comments	House View
Cash	Money market swap rates are improving but interest rates remain low but it is too soon to become overweight.	NEUTRAL
UK Corporate Bonds	Our view of this asset class has moderated recently but there is still value to be had. The greater opportunity present in high yield bonds comes with risk comparable to equities.	OVERWEIGHT
UK Index Linked	Five year yields remain fairly valued. The emergence of inflation could change our view in the future.	NEUTRAL
International Corporate Bonds	Fluctuating exchange rates makes these funds which hedge against currency risk more expensive.	NEUTRAL
UK Gilts	Yields have pushed up sharply over fears of excessive issuance. Future inflation will place more pressure on this asset class.	UNDERWEIGHT
UK Equities	Corporate earnings are sector dependent. The UK stockmarket is supported by a relatively high oil price.	NEUTRAL
European Equities	Continue to look good value. Euro has weakened against Sterling but several factors could hold back recovery.	UNDERWEIGHT
North American Equities	First economy into recession and looks set to be first out. Questions over whether recent rally is really sustainable.	OVERWEIGHT
Japan Equities	Recent rally set a record quarterly gain but equities in this asset class are costly compared to European and the UK.	NEUTRAL
Asia ex-Japan Equities	Companies on MSCI Asia Pacific Index currently trading at 24 times estimated net income which is quite costly compared to Europe.	NEUTRAL
Emerging Market Equities	Our view remains more optimistic than for developed markets. Many risks to consider.	OVERWEIGHT
Property	Cost of funding might be increasing but availability of credit also improving. Could be more bad news to come.	UNDERWEIGHT

The terms 'overweight', 'neutral' and underweight represent our view of tactical asset allocation adjustments to a well diversified strategic portfolio.

## The Small but Important Print

We have tried to minimise the use of jargon and technical terms in this document to make it more readable whilst also containing some worthwhile information.

This attempted simplification inevitably means that some caveats must be added to ensure that the limitations of the document are clearly stated:

- Past performance is not necessarily a guide to the future. The value of investments can go down as well as up.
- The value of tax concessions depends on your circumstances and may change.
- All assumptions and estimates are approximate and intended to serve as initial guidelines only. You should seek professional independent financial advice before making any investment decision.
- This report is based on our understanding of current economic and market conditions combined with our knowledge of legislation and HM Revenue and Customs. All of these may change in the future and affect the suitability of any financial arrangement.
- Regular reviews of all financial arrangements should be undertaken to review progress and make adaptations where necessary.
- Informed Choice Ltd is authorised and regulated by the Financial Services Authority.